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Nos. 86-781 and 86-793

In the Supreme Court of the United States

OCTOBER TERM, 1986

KANSAS GAS AND ELECTRIC COMPANY,
Appellant,

vs.

STATE CORPORATION COMMISSION OF
THE STATE OF KANSAS,
Appellee.

KANSAS CITY POWER AND LIGHT COMPANY,
Appellant,

vs.

STATE CORPORATION COMMISSION OF
THE STATE OF KANSAS,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF KANSAS

MOTION BY THE STATE CORPORATION COMMISSION OF THE STATE OF KANSAS TO DISMISS KANSAS GAS AND ELECTRIC COMPANY FOR LACK OF A CASE OR CONTROVERSY

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Pursuant to Rule 42 of the Rules of the United States Supreme Court, Appellee State Corporation Commission of the State of Kansas (KCC or Commission) respectfully moves this Court to dismiss Case No. 86-781, the appeal of Kansas Gas and Electric Company (KG&E), for mootness, or a lack of a case or controversy.

STATEMENT OF THE CASE

This matter involves consolidated appeals by Kansas City Power and Light Company (KCPL) and the Kansas Gas and Electric Company from orders of the State Corporation Commission of the State of Kansas concerning interim rates associated with Kansas' first nuclear generating station, Wolf Creek. The Kansas Supreme Court affirmed the Commission's orders in *Kansas Gas and Electric Co. v. Kansas Corporation Commission,* 239 Kan. 483, 720 P.2d 1063 (1986), reh'g denied, July 17, 1986. The United States Supreme Court noted probable jurisdiction on February 23, 1987.

ARGUMENT AND AUTHORITIES

It is well settled that federal courts may act only in the context of a justiciable case or controversy. *Benton v. Maryland,* 395 U.S. 784, 788 (1969). The lack of jurisdiction to review moot cases derives from the requirement of Article III of the Constitution under which the exercise of judicial power depends upon the existence of a case or controversy. *Liner v. Jafco, Inc.,* 375 U.S. 301, 306 n.3 (1964). Indeed, a controversy must exist at all stages of appellate review, and not merely at the beginning of the action. *S.E.C. v. Medical Committee for Human Rights,* 404 U.S. 403 (1972). No such justiciable controversy now exists as to KG&E's appeal because recent developments before the KCC have substantially altered the relevant facts.

In its appeal to this Court, KG&E alleges the 1985 Wolf Creek rate orders violated its constitutional rights by setting confiscatorily low rates and denying it equal protection and due process of law. However, the 1985 Wolf

Creek order was interim in nature. It was well understood by all parties that a permanent rate case would be heard subsequently. In the case of Appellant KG&E, a permanent rate proceeding was held and the attached order issued. KG&E neither requested rehearing nor appealed the order, and with good reason. The current order granted virtually all that it requested. (KG&E Jurisdictional Statement, p. i) Thus, KG&E's rates are not based on the 1985 order, which was interim in nature, but rather on an order issued by the Commission on March 11, 1987.[1] The recent "permanent" order has results which allow substantial improvements in KG&E's finances, delays previously authorized rate increases and reduces the space heating rate, all as requested by KG&E. Significantly, that order also provides for a 5 year phase-in of the Wolf Creek physical excess capacity and amortization of the costs previously found imprudent. (Appendix, p. A26, ¶ 41, p. A31, ¶ 44) Furthermore, the March 11th order contains a valuation of the Wolf Creek plant at its full "prudent" original cost rather than the valuation method forming the basis for KG&E's equal protection and due process contentions. Consequently, there is no legal or factual basis for appeal of the original interim order since any review by this Court would have no effect on KG&E's rates or earnings. Significantly, KG&E's witness in the permanent rate proceeding reached the same conclusion when he maintained that the Wolf Creek appeal in this court would not change nor alter the strategy of KG&E in reestablishing its financial health. (Transcript attached as Appendix)

As is customarily true of initial changes in rates due to completion of large electric generating plants, the

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1. Order in Docket Nos. 142,098-U and 149,109-U attached as Appendix.

original Wolf Creek orders were interim in nature.[2] Because those interim rates were based upon estimated data, permanent rates were not to be established until six months of historical data was gathered from the operation of Wolf Creek. However, in addition to requesting that its rates be made permanent, KG&E on December 9, 1986, requested Commission approval of a "rate stabilization overall plan" consisting of a number of interrelated accounting, financing and rate elements which it believed would benefit both ratepayers and investors.

In its rate stabilization plan KG&E urged the Commission to (a) revalue Wolf Creek at $2,376.00 per KW; (b) approve a mechanism which would allow all of Wolf Creek capacity to be recognized in rates by 1992; (c) delay approximately $80 million in rate increases already approved by the Commission;[3] and (d) lower, by approximately $6 million per year, the space heating rate currently on file with the Commission. In addition, KG&E requested various accounting changes and prospective rate findings. KG&E also requested Commission approval to purchase "key-man" life insurance, and dedicate an $800 million income stream generated by these insurance policies to Kansas jurisdictional cost of service.

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2. Interim rates are rates subject to change or adjustment. Traditionally the adjustments are performed in the next permanent rate case. The Commission's rationale for making KG&E's rates interim is found in the Joint Appendix, p. 122c-123c.

3. In the initial case concerning Wolf Creek, KG&E, as well as a number of intervenors and staff, proposed a variety of phase-in plans. The Commission ultimately adopted a four step, nine year phase-in, which had interim rate increases due on September 27, 1987, and September 27, 1988. The KG&E plan proposed delaying the September 1987 phase-in increase until January 1, 1989, and delaying the September 1988 increase until January 1, 1992. The revenue increases which KG&E would have received if the original phase-in were followed, and which will be foregone under the plan, amount to approximately $80 million. (Appendix, p. A17, ¶ 32)

With slight modifications, the Commission approved KG&E's plan on March 11, 1987. The permanent rates now in effect are, therefore, based upon the March 11th order, insofar as this appeal is concerned. The 1985 orders simply have no relevant legal effect on KG&E's current rates, having been superseded in all material respects by the March 11, 1987 order. Although the 1985 order made many determinations on various cost of service components, such as operation and maintenance expense and decommissioning costs, which are reflected in current rates, there is no dispute between the parties concerning the lawfulness or reasonableness of those findings. Rather, it is the 1985 treatment of Wolf Creek capital costs which is the focus of KG&E's appeal. That treatment, however, is no longer in effect. Thus, continued Court review of the 1985 Wolf Creek order would have no effect on KG&E's rates, and would not be in the interest of judicial economy.

It may be argued by Appellant that this case is not moot because it represents an issue capable of repetition, yet evading review. *Moore v. Ogilvie,* 394 U.S. 814 (1969); *Roe v. Wade,* 410 U.S. 113 (1973) Interim utility rate orders may sometimes be superseded by permanent rate orders before judicial review is completed. However, it is not necessary in this case to address generally the question of mootness in such situations. Clearly, this is not a a situation which is capable of repetition in the normal course of events. In this instance, the specific basis for each of the issues on appeal has been completely changed by the subsequent order making rates permanent. Furthermore, the March 11, 1987 Commission order contemplates that the framework it establishes will govern the setting of KG&E rates for the remaining operational life of Wolf Creek.

As reflected in the March 11, 1987 order KG&E anticipates no future rate increases associated with Wolf Creek

capital costs other than those provided for by the plan. (Appendix, p. A11, ¶ 23) This is because the plan allows for adequate future returns on KG&E's investment. Due to the accounting, ratemaking and other changes authorized by the Commission, KG&E projects that it will earn a return on equity in the next ten years which will range between 8.69 percent to 10.39 percent. (Appendix, p. A14, ¶ 26) This projection includes return on equity associated with Wolf Creek costs which the Commission found to be imprudently incurred. (KG&E is not appealing that Commission determination.) In conjunction with the fact that KG&E stock recently sold at $23.50 a share, a ten year high, and its expected 1986 dividends are $1.40 a share, it is thus evident why KG&E's plan requires no additional rate increases. (Appendix, p. A14, ¶ 26)

The preceding facts also demonstrate that the Commission's approval of KG&E's plan has rendered moot KG&E's contentions of confiscation. The end results of the balancing of investor and consumer interests required by *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1944), were significantly different in the Commission's March 11th order than its 1985 orders. Under the March 11th order, KG&E investor interests were substantially benefitted—albeit without a major increase in rate.[4] Perhaps most telling to the continuing vitality of KG&E's *Hope* argument, however, is the fact that the rate levels now in effect and end results of those current rates are precisely those requested by KG&E. Quite simply, the balance achieved by current rates under KG&E's plan are evidently satisfactory to the company.

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4. KG&E's plan seems to be based in large part on recognition that its rates are high and that the company's financial health is inextricably tied to making its electric service affordable and useful to consumers. (Appendix, p. A12, ¶ 24) Thus, the delays in scheduled rate increases and reduction in space heat rates are designed to avoid loss of customers.

The legally operative facts relating to KG&E's equal protection and due process claims have also changed. Both those claims arise from the Commission's valuation of Wolf Creek in the 1985 order at $1290 per kilowatt of capacity. The March 11th order, however, changed that valuation to $2376 per KW. Since that new valuation represents Wolf Creek's original prudent cost, which KG&E argues is required by the equal protection clause there is no longer an issue on that claim. Further, since the new value of Wolf Creek is at the figure requested by KG&E, there is no longer any basis for KG&E's claim that it received inadequate notice in violation of its due process rights.

CONCLUSION

KG&E's appeal to this Court is moot because the appeal was based upon an interim rate order, which has been superseded by the permanent rate order. In addition, every aspect of the original, interim order which KG&E alleges was constitutional infirm has now been changed in the permanent rate order to reach results which KG&E urged in its recent rate application. Consequently, no issue, case, or controversy exists between KG&E and the KCC.

Respectfully submitted,

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APPENDIX

(Filed March 11, 1987)

THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Michael Lennen, Chairman
Margalee Wright
Keith R. Henley

In the Matter of the Application of Kansas Gas and Electric Company for Approval of a Plan to Delay or Reduce $100 Million of Approved Rate Increases, Sustain KG&E's Progress in Restoring Its Financial Health, Establish a Framework for Rate Recognition of KG&E's Prudent Investment in Wolf Creek, and Amortize KG&E's Commission Determined Imprudent Investment in Wolf Creek.	)	Docket No. 142,098-U 84-KGE-197-R
In the Matter of the Application of Kansas Gas and Electric Company Requesting that Interim Charges for Electric Service Be Made Permanent.	)	Docket No. 142,098-U 84-KGE-197-R
In the Matter of the Application of Kansas Gas and Electric Company for an Accounting Order Relating to the Amortization of AFDUC Related Tax Credits and Accounting for the Debt Component of AFUDC and Deferred Carrying Charges.	)	Docket No. 149,109-U 86-KG&E-3-A

ORDER

NOW, before the State Corporation Commission of the State of Kansas, come for consideration and determination the Applications of Kansas Gas and Electric Company (KG&E) in Docket No. 142,098-U, for approval of a plan to delay or reduce $100 million of approved rate increases, sustain KG&E's progress in restoring its financial health, establish a framework for rate recognition of KG&E's prudent investment in Wolf Creek, and amortize KG&E's Commission determined imprudent investment in Wolf Creek; a request that interim charges for electric service be made permanent; and, in Docket No. 149,109-U, an accounting order relating to the amortization of AFUDC related tax credits and accounting for the debt component of AFUDC and deferred carrying charges and, further, the motion of KG&E to consolidate Docket Nos. 142,098-U and 149,109-U.

I. *Appearances*

The following parties entered an appearance in the above captioned matters:

For the Applicant/Movant, KG&E,

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Wichita, Kansas 67201-0208

For the Kansas Corporation Commission Staff and the public generally,

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For Kansas Power and Light Company:

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For the Alliance for Liveable Electric Rates:

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For the City of Wichita:

Joe Allen Lang
Office of the City Attorney of
Wichita, Kansas
Department of Law
City Hall, Thirteenth Floor
Wichita, Kansas 67202

At the hearing, the following witnesses testified:

On behalf of KG&E

Mr. James S. Haines, Group Vice President
Mr. E. D. Prothro
Mr. Earnest A. Lehman
Mr. Dick Rohlfs

On behalf of Staff

Mr. Bion C. Ostrander
Mr. Ganesh Krishnan

On behalf of Industrial Intervenors

Mr. Fred B. Adam

On behalf of Electric Shock Coalition

Ms. Mary Abbott Mills

II. *Findings of Fact and Conclusions of Law*

Having considered the evidence and testimony, the files and records, and being fully advised in the premises, the Commission finds and concludes as follows:

1. KG&E is a corporation under the laws of the State of Kansas with its principal place of business at 201 North Market Street, Wichita, Kansas. KG&E is an electric "public utility" within the meaning of K.S.A. 66-104 and is authorized to engage in the business of an electric "public utility" in the State of Kansas.

2. Notice of the above captioned applications and the Motion to Consolidate these applications and hearings were given to all parties of record and published in newspapers of general circulation in the service area. The Commission finds that notice is proper and that the Commission has jurisdiction to consider this matter.

3. KG&E filed its Application Requesting Proposed Changes in Charges for Electric Service in Docket No. 142,098-U on November 8, 1984. That Application requested an increase in KG&E's rates to cover a test year revenue deficiency of $373,427,835, principally due to the commercial operation of the Wolf Creek Generating Station (Wolf Creek), of which KG&E owns a 47 percent interest.

4. After lengthy technical and public hearings, the Commission issued Orders in Docket No. 142,098-U on September 27 and November 15, 1985 (Wolf Creek rate Orders). In those Orders, we determined that KG&E's 1985 test year revenue deficiency was $169.6 million, before fuel savings estimated to be between $25 million and $28 million, and ordered that a corresponding increase be phased into rates in four steps, as follows:

Year	Amount (Millions)	% Increase
1985	$135.00	37%
1986	20.0	4
1987	14.6	3
1988	15.6 (5 years to cover deferred phase-in revenues)	3

5. The first increase became effective on October 3, 1985 and the second increase became effective on September 27, 1986. Both increases went into effect on an interim basis and, with its July 25, 1986 Application Requesting That Interim Charges For Electric Service be made Permanent in Docket No. 142,098-U, KG&E has requested that such increases be made permanent.

6. In our September 27, Wolf Creek rate Order, we recognized that granting KG&E less than it requested could have a serious impact on KG&E's financial health.

7. In response to the Wolf Creek rate Orders, KG&E took a number of cost saving measures. KG&E cut its common dividend in half, eliminated 200 jobs, cut 20 percent of its construction budget, froze officers' salaries, eliminated management incentives, greatly reduced civic and charitable contributions, curtailed involvement in industry and professional associations, and initiated cost control measures over many expenditures not necessary in providing direct customer service. Additionally, KG&E has engaged

in extensive refinancing to both lower its embedded cost of debt and retire a majority of its preferred stock.

8. While KG&E's cost cuts and economic refinancings have lessened the financial impact of the Wolf Creek rate Orders, KG&E believes that these changes have not established sustainable progress toward the restoration of its financial health. Toward that end, in Docket No. 149,109-U, KG&E asked the Commission to approve two accounting changes which would improve KG&E's financial condition without an immediate need for a rate increase. KG&E sought Commission approval to (a) accelerate the amortization of construction related tax credits to an eight year schedule, rather than over the entire depreciable life of the property which gave rise to the credits, and (b) capitalize the deferred carrying charges that the Commission permitted with respect to KG&E's physical excess capacity in Wolf Creek using a before tax (gross) rate of return for preferred stock and long term debt rather than the current net of tax rate.

9. Our March 12, 1986 Order in Docket No. 149,109-U approved the accelerated amortization of construction related tax credits, while deferring action on the proposal dealing with deferred carrying charges.

11. KG&E has also acted to retain its existing sales base by negotiating to prevent the loss of major customers for whom, during the present period of time when KG&E has a large surplus of generating capacity, cogeneration presents a cost savings opportunity at the expense of other customers. Significantly, KG&E has made no effort to shift to other classes of customers the revenue shortfall which has resulted from the negotiation of special rate contracts. Such shortfall, which has been reasonably estimated to be $4 million over the 5-year term of the contracts,

is material and it diminishes the beneficial impact of the steps KG&E has taken to improve its financial situation.

12. On December 9, 1986, KG&E filed an Application in Docket No. 142,098-U in which it requested approval of a Plan which it contends will permit continuation of its efforts to improve its financial condition while permitting customers to save approximately $100 million over the next five years. KG&E describes the Plan as having four interdependent components: (a) approximately $100 million of delays in previously granted rate increases and reductions in certain rates to enhance the economic viability of KG&E's service territory and efficient use of KG&E's generating facilities, (b) a basis to sustain KG&E's progress in restoring its financial health, (c) a specific framework for the rate recognition of KG&E's prudent investment in Wolf Creek, and (d) amortization of KG&E's imprudent investment in Wolf Creek. At hearing, Mr. Deaver requested and was granted leave to make three oral amendments to KG&E's December 9 Application.

13. KG&E's proposed Plan depends on an approximate $800 million stream of income in excess of premium expense which KG&E expects to receive over the next 40 years as the owner and beneficiary of life insurance policies on 82 of its directors, officers and key employees. KG&E states that the life insurance policies will be funded entirely by KG&E's shareholders. KG&E proposes to combine this stream of income with utility operating revenue to cover its jurisdictional cost of service in Kansas, including a return on its prudent investment in Wolf Creek.

14. KG&E states that its Plan will permit a delay from September 27, 1987, to January 1, 1989, of the third increase approved in the Wolf Creek rate Orders. A pending issue before the Commission in Docket No. 142,098-U

at the time the KG&E application was filed was whether it was reasonable and prudent for KG&E to retire its Ripley Station. KG&E requests that the revenue impact of this issue be added to the third increase, as delayed. Under its Plan, KG&E also proposes a delay from September 27, 1988 to January 1, 1992 the fourth increase approved in the Wolf Creek rate Orders. That increase was approved as a temporary five year increase, and KG&E has requested that it be approved as a permanent increase. Under KG&E's Plan these delayed third and fourth rate increases would be approved now, and become effective on a permanent basis on January 1, 1989, and January 1, 1992, respectively, and to be spread on an equal percentage basis to each component of each rate schedule. KG&E believes that these proposed delays, if adopted, would save KG&E's customers approximately $80 million over the next five years. KG&E believes the remaining $20 million of customer savings over the next five years would come from the proposed reduction to 5¢ of its current rate of 7.14¢ per KWH for residential and farm electric space heating customers' usage above 500 KWH per month during the non-summer months (all months except June, July, and August). We note that KG&E suggested at hearing that its December 9, 1986, Application understates the customer savings from this proposed reduction. The company contends that the savings over the next five years is more likely to be $27 million, as the annual savings are expected to be $5.4 million.

15. KG&E states that the viability of its Plan requires that it be permitted to retain the benefits of its cost-cutting measures, economic refinancings and the savings due to the new federal tax law. Further, KG&E requests that the Commission reconfirm one accounting change and authorize two others: (a) accelerate to eight years the amortization of construction related tax credits,

as already approved in our March 12, 1986 Order in Docket No. 149,109-U, and (b) accrue carrying charges on the portion of Wolf Creek which constitutes physical excess capacity at KG&E's 4.91 percent before tax (gross) weighted cost of debt rate applied to KG&E's investment of $2,376 per KWH with this accrual to cease December 31, 1991, and capitalize an 11.995 percent before tax (gross) return on deferred phase-in revenues, with such accruals to be amortized on a sinking fund basis over Wolf Creek's remaining depreciable life, and (c) extension of Wolf Creek's depreciable life to 40 years for a composite annual depreciation rate of 2.61 percent for its share of Wolf Creek.

16. KG&E's December 9, 1986, Application in Docket No. 142,098-U also restated KG&E's July 25, 1986, request that the first and second increases under the Wolf Creek rate Orders, presently in effect on an iterim basis, be made permanent.

17. KG&E also requests that it be permitted to amortize over five years the $6.4 million deferred asset which represents the allowed costs of operating Wolf Creek from the commercial service date to the effective date of the Wolf Creek rate Orders.

18. KG&E's Plan further would have us find, under the methodology of the Wolf Creek rate Orders, that the excess portion of KG&E's Wolf Creek capacity currently is 269 MW and that KG&E estimates this excess should be reduced by 53.8 MW on January 1 each year from 1988 through 1992, so that KG&E would stop accruing deferred carrying charges on excess capacity by December 31, 1991, and then begin amortizing the accrued charges by January 1, 1992. KG&E has also proposed that if we later determine the retirement of Ripley Station to have

been reasonable, the amount of excess capacity should be reduced by 46 MW to 223 MW and the annual reduction should be 44.6 MW.

19. Under its Plan, KG&E would accrue deferred phase-in revenues with carrying charges based on an 11.995 percent before tax (gross) rate of return, compounded semi-annually, until such time as the delayed third rate increase becomes effective, and then accrue the carrying charges on accumulated deferred phase-in revenues until the delayed fourth rate increase becomes effective. At that time the amortization of the accruals on a sinking fund basis over Wolf Creek's remaining depreciable life would begin.

20. Finally, KG&E's December 9, 1986 Application in Docket No. 142,098-U requests that we permit KG&E to amortize above the line, in cost of service, and over Wolf Creek's remaining depreciable life the undepreciated portion of the $128 million of KG&E's investment in Wolf Creek which we have found to be imprudent, and then find that the Plan permits rate recognition of KG&E's investment in Wolf Creek beginning January 1, 1992.

21. Due to the interrelationship of the accounting authority requested by KG&E in Docket No. 149,109-U and the Plan set out in KG&E's December 9, 1986, Application in Docket No. 142,098-U, we find that it is appropriate and reasonable to consolidate Docket No. 149,109-U with Docket No. 142,098-U.

22. The KG&E Plan contains many elements, which are each addressed below. Although we approve of each of the Plan's individual elements with some modifications, it should be noted at the outset that many of those elements, standing alone, would likely not normally receive

Commission approval. It is only within the context of the total Plan that we sanction all the separate components. As discussed below, each element of the Plan has real or potential benefits or detriments for ratepayers. Indeed, many elements have effects which vary over time so that they cannot be characterized as wholly beneficial or detrimental to ratepayers. For example, the accounting changes decrease the costs of service during the early years of the Plan, but increase them in later years. On the other hand, the income from the life insurance policies will not be significant in the early years of the Plan, but increase gradually to over $30 million in the later years. Because the effects of the individual elements of the Plan vary over time, so do the net combined effects. In any given year, of course, the net effect of the Plan can be determined, but we have focused more on the totality of the Plan and its potential benefits for both ratepayers and KG&E.

23. The primary benefits of KG&E's Plan, from the perspective of ratepayers, is the deferral of already authorized rate increases, a rate decrease for space heat customers and the likelihood of no additional rate increases related to Wolf Creek capital costs other than those provided for by this order. This Plan contemplates only one rate change which was not explicitly envisioned by our original Wolf Creek orders, the $15.6 million fourth step permanent increase, which was originally to terminate after five years once carrying costs on deferred phase-in revenues were recovered. As noted below, however, the continuation of the rate increase in 1998 may well be justified by greater need for Wolf Creek capacity in any event. In fact, greater or additional rate increases due to changes in circumstances expressly contemplated in our original order, such as capacity additions or a valuation

adjustment, would be a real possibility. However, the Plan would permit ratepayers to avoid such rate increases. As Mr. Haines testified, ". . . the Plan permits rate recognition by January 1, 1992, of KG&E's prudent investment in Wolf Creek such that, assuming reasonable circumstances, no further rate increases will be needed as the amount of Wolf Creek considered to physically excess is reduced or as coal capacity, becomes more expensive." (Haines, Tr. 61). Not only does the Plan forestall indefinitely rate increases due to Wolf Creek capital costs, but also delays for a significant time the need for rate increases due to other cost increases. As stated by KG&E witness Haines, the Plan provides "a very good probability" that no rate increases would be necessary in the next five to ten years for increases in costs of service other than Wolf Creek. (Haines, Tr. 113).

24. The delays in previously scheduled rate increases and the reduction in the space heat rate obviously provide real benefits to rate payers but they are also beneficial to KG&E. Thus, Mr. Haines explained the proposed rate delays and reduction as KG&E recognition "that its health is inextricably tied to the health of its service territory. Economically efficient use of KG&E's generating facilities results from making KG&E's electric service affordable and useful." (Haines, Tr. 53). The Commission continues to be concerned about the level of KG&E's rates. KG&E, along with KCPL, have by far the highest rates in Kansas of a generating utility and the highest retail rates of an investor owned utility. Furthermore, those rates are significantly above the normal average. It was thus not surprising that KG&E witness Lehman stated that KG&E's principal means of encouraging conservation is through its "overall rate level, which is high." (Lehman, Tr. 337). Although Mr. Lehman was being partially facetious, it is

a fact that KG&E's rates are high. It is encouraging that KG&E now recognizes the need to keep rates reasonable, not only for the sake of ratepayers but also for the good of the company. The possibility of real rate stability with limited future rate increases consequently leads us to conclude that the Plan as a whole is acceptable.

25. Before turning to the individual elements of the Plan, we should further address some of the overall concerns about the Plan. Because of the requested treatment of Wolf Creek capital costs and the requested accounting charges, KG&E's revenue requirements under traditional rate making would theoretically increase in the future. KG&E, however, asserts that any and all such increases would be covered by the income from the insurance policies. Because the projected income of $800 million is a net of tax amount, it will supplant a much greater incremental amount if analyzed in terms of revenue requirements. It is this feature of the Plan which allows for the promised rate stability and further persuades the Commission to allow retention of the income tax and other cost reductions. Without such long term contributions from the shareholders, it would be inequitable for ratepayers to totally forego the benefits of the income tax and other cost reductions, while also facing ratemaking and accounting changes which theoretically increase future revenue requirements. KG&E witness Haines also responded to staff concerns about the large revenue requirements created by the Plan. He noted that KG&E's earnings under the Plan are better than under conventional ratemaking treatment. Furthermore, he stated that KG&E could not automatically come in and obtain conventional rate recognition of 100 percent of its prudent investment in Wolf Creek and the Plan was approved. "When the reasonable rate doctrine is considered, it is very probable that at least

over the next 10 years, KG&E would not be permitted to charge any higher rate with the Plan than without it." (Haines, Tr. 476-77).

26. The other threshold question before the Commission is whether KG&E does, in fact, require its requested changes in order to "restore its financial health." We noted previously that KG&E has taken several measures to reduce its costs in order to cope with our 1985 orders. However, the record indicates those orders have not had consequences as dire as predicted by some. KG&E stock has recently been selling at $23.50 a share, a ten year high. Although the expected earnings per share for 1986 is around $1.40, down from $2.13 in 1985 due to cessation of AFUDC, KG&E believes that "Relative to where we were a year ago, we're certainly doing quite well and we are pleased with that." (Haines, Tr. 74). Nonetheless, the Commission does agree that improvement in KG&E's financial picture is desirable for all concerned if it can be accomplished at a reasonable cost to ratepayers. Indeed, the Commission has previously taken a step in that direction in approving the accelerated amortization of construction related tax credits. Under the KG&E Plan, the company projects that it will be able to earn a return on total equity, including equity associated with Wolf Creek costs found to be imprudent, which will range between 8.69 percent and 10.39 percent for the ten years period of 1986 through 1995. KG&E suggests that these are "minimally adequate" returns but also notes that it is exploring other mechanisms, such as a sale-lease back arrangement, which will further improve its situation. Although the Commission would not necessarily agree that those projected returns are "minimally adequate," especially since they include a return on imprudent investment, we do agree that there should be no need for further

rate increases related to Wolf Creek capital costs with such returns.

27. The first individual element of the Plan is the life insurance plan. KG&E will be permitted to combine its projected $800 million stream of income from corporate owned life insurance over the remaining life of Wolf Creek with utility operating revenue to cover KG&E's Kansas jurisdictional cost of service, including a return on KG&E's investment of $2,376 per KW in Wolf Creek. Some questions were raised concerning the amount KG&E would actually receive, as well as the certainty of KG&E actually receiving the $800 million over the next 39 years. Witnesses for KG&E testified that this is a conservative or worst case projection. Indeed, Mr. Prothro testified that under more favorable assumptions, KG&E could receive as much as a billion dollars. A potential significant risk, according to KG&E, is a change in federal tax laws which would adversely affect the insurance policies, although we note that tax law changes have traditionally been prospective in nature, as opposed to retroactive in nature. The utilities we regulate are always subject to the risk of future laws which would upset previous assumptions concerning cost of service. However, in view of the potential benefits to customers and shareholders of KG&E, we consider this risk to be reasonable. Consistent with its proposal, KG&E is directed to fund the corporate owned life insurance exclusively with shareholder funds. Normally it is not permissible to combine income from shareholder funded, non-utility assets with utility operating revenue to cover the cost of providing regulated utility service. In this case, however, we find that it is appropriate because KG&E has requested such treatment, and KG&E's shareholders will benefit from other aspects of the Plan.

28. KG&E is permitted to delay from September 27, 1987 to January 1, 1989 the third increase previously approved in the Wolf Creek rate Orders. In a separate Application in Docket No. 142,098-U, the Commission has determined that it was reasonable and prudent for KG&E to retire its Ripley Station. The Commission directs that the revenue impact resulting from the Ripley retirement be added to the third increase and become effective on a permanent basis on January 1, 1989, with one condition. KG&E also requested that such incremental revenue impact be accounted for from September 27, 1985, until January 1, 1989, as deferred phase-in revenues. Although we found the Ripley retirement was reasonable, the evidence does not support this aspect of KG&E's Plan. KG&E's actual normalized peak in 1986 was 40 MW below its forecasted peak. Consequently, we cannot find that it is reasonable to permit KG&E to accrue deferred phase-in revenues for an additional 46 MW of Wolf Creek to balance the loss of 46 MW from Ripley. At the same time, it is reasonable to assume that KG&E's need for Wolf Creek, whether from peak growth or reduced overall generating capability, will have grown by 41 MW from 1986 to 1988 so as to justify adding the incremental revenue impact to the January 1, 1989, increase. Also, as a condition precedent to the inclusion of revenues associated with the Ripley retirement in the January 1, 1989, rate increase, we direct the company to show the Commission that this demand growth or reduced overall generating capacity has occurred. Additionally, the revenue impact should be determined using an overall cost of capital equal to KG&E's rate of return on deferred revenues as of January 1, 1989, as set forth in paragraph 31, and should reflect Wolf Creek's accumulated reserve for depreciation as of January 1, 1989.

29. KG&E has requested the authority to delay from September 27, 1988 to January 1, 1992, the fourth increase of the phase-in approved in the Wolf Creek rate orders. When both the third and fourth increases are delayed, KG&E customers will save approximately $80 million. This particular portion of KG&E's plan is definitely beneficial to ratepayers. KG&E is permitted to delay the fourth increase, as requested.

30. KG&E's request to spread the third and fourth increases on an equal percentage basis to each component of each rate schedule is approved as being fair and reasonable. This method of rate design is consistent with the previous Wolf Creek Orders, and staff did not object to this method of spreading these increases.

31. KG&E is directed to capitalize the delayed revenue increases and a rate of return on such deferral using the before tax (gross) method. The rate of return on deferred revenues shall reflect KG&E's actual weighted cost of debt and preferred as determined annually from its official annual report to the Commission (Form No. 1). The authorized return on common equity will remain at 15.5 percent. The return on deferrals shall be compounded semi-annually. Staff witness Mr. Ostrander testified that the September 27, 1985 Order in Docket No. 142,098-U does not permit semi-annual compounding. While we tend to agree with staff that the language of the Order at paragraph 8 on pages 133 and 134 does not permit semi-annual compounding, we can understand the company's belief that the language is ambiguous. However, the only question before us today is whether KG&E may semi-annually compound the deferrals. We hereby grant specific authority for KG&E to do so.

32. KG&E, in its application, requests that it be permitted to place the third and fourth increases of the

phase-in of the Wolf Creek rate order into effect on a permanent basis. The Commission notes at the outset that it is normally hesitant to grant permanent rate increases such as the increases contemplated by KG&E's Plan, on a prospective basis. In the regular rate making setting such a prospective treatment normally includes a great deal of speculation due to the nature of the future. However, it should be noted that as part of the original Wolf Creek Order, the Commission has already granted the third and fourth phase-in steps on a interim basis. Indeed, the Commission approved the interim steps to become effective in 1987 and 1988. The Commission notes with approval the company's plan to delay these increases until 1989 and 1992. The Commission believes that these deferrals are a true benefit to the consumers of KG&E's services. Both staff and the company seem to agree that the benefit of the delays in the third and fourth rate increases will result in a savings to KG&E customers of the magnitude of $80 million. Thus, in light of the delay that KG&E is willing to accept in delaying the increases in balance with other portions of the plan, the Commission believes it is reasonable to allow KG&E to file tariffs showing that the third and fourth phase-in increases are permanent increases. However, we note by this action that we have not foreclosed the possibility of further challenge to the third and fourth increases. Nor is our action inconsistent with the possibility that at some point after the increases become effective that it would be appropriate to examine the reasonableness of KG&E's earnings. Indeed, it is likely that the Commission will wish to review this aspect of the plan in the latter part of the next decade. If no earlier action is necessary, any customer of KG&E, as well as the Commission staff, is always free to file a complaint alleging that KG&E's rates are unreasonable. It should be noted, as stated in other parts of this order, that the Commission

believes the increases should be spread on an equal percentage basis to all components of each rate schedule.

33. KG&E, through Mr. Lehman, presented evidence which suggests that, at its present rate of 7.14¢ per KWH for residential and farm electric space heating customer's usage above 500 KWH per month during non-summer months (all months excepting June, July and August), KG&E will gradually lose space heating load. Thus in the instant application, KG&E has proposed to reduce its residential and farm space heating rate from the current 7.14¢ to 5.00¢ per KWH for all KWHs in excess of 500 KWHs. In addition, KG&E has indicated that if its proposed reduction is approved, it will not seek to recover the short run revenue loss from other customers. However, if the proposed reduction is not approved, KG&E believes that over the next ten years the loss of revenues and market share will grow to significant levels.

KG&E's evidence at hearing showed that the proposed reduction to 5¢ per KWH would result in a revenue loss of approximately $5.4 million in the first year of reduction, but within 6 to 7 years would result in greater revenues than would have been produced had the 7.14¢ per KWH rate remained in effect. The Staff, through its witness Dr. Krishnan, found substantial problems with the method and model used for estimating KG&E's revenue loss by Mr. Lehman. Dr. Krishnan found that in the econometric model used by KG&E one of the variables, specifically the gas-to-electric price ratio variable, was not statistically significant and in no way furthered the econometric model's reliability. Indeed, Dr. Krishnan testified that the gas to electric price ratio variable was statistically insignificant. Additionally, Dr. Krishnan believes that the perfect inelasticity of demand contained within the econ-

ometric model was an unrealistic assumption. While we find that Staff's evidence as to the econometric model to be reasonable, we note that KG&E's willingness to forego recover the short-run revenue loss from other customers, and in effect underwrite that loss itself, is a significant factor in favor of this particular component of the Plan. Thus, the Commission finds that the reduction in space heating rate to 5.00¢ per KWH reasonable. But, the Commission recognizes that the proposed cut-off of 500 KWH is, in reality, a substitute for accurate metering. A more realistic cut-off figure above which the space heating rate would apply in 650 KWH. Therefore, for all residential consumers who are eligible for the space heating rate, the cut-off will be 650 KWH. However, an exception shall be all-electric apartments. Apartments average a lower kilowatt per hour use, and therefore the space heating cut-off for apartments should be set at a lower rate, 500 KWH. Therefore, the space heating rate reduction is approved, and the reduction will be allowed for usage over 650 KWH for residential, and 500 KWH for residential apartments.

The Commission also recognizes the lack of specific use data on space heating, and further, that the cut-off levels as specified do not reflect precisely space heating use. The lack of accurate metering is a problem when implementing targeted-use rates. Therefore, an investigation shall be commenced by the Commission to look at the benefits of separate metering. Also, the specific usage information on space heating shall be gathered by KG&E, and the cut-off levels re-evaluated in the above referenced investigation.

34. The Commission has a number of other concerns of a general nature with the reduction of the space heating rate. The Commission notes that in reducing the

rates the company has set out on a plan that could be construed as being contrary to long term planning and conservation. This Commission and the company have a significant interest in the long term planning and conservation of utility resources in Kansas. It is understandable that KG&E plans to aggressively market their product and try to sell more electricity. Indeed, growth may be a desirable goal. However, it appears that KG&E's goal extends past space heating; it wishes to increase the number of all electric homes and apartments. (KG&E Servicegraph, Vol. 52, Issue 12, Dec. 1986). While this goal is understandable, it makes the Commission's role as overseer of the public interests even more important. Thus, the Commission believes that it must mandate conservation and load management goals as a part of this docket. We must make sure that the growth that does occur is efficient, planned growth. It is important that the approval of the space heating rate be seen for what it is; an attempt to target a specific use of electricity that will increase off-peak load, and therefore overall efficiency. The Commission wishes to specifically note that its space heating findings in this docket is not a signal for any utility to unreasonably market its product which would ultimately increase its peak demand.

35. As part of its Plan, KG&E has requested that it retain the benefits resulting from its cost cutting measures. KG&E, through Mr. Haines and Mr. Prothro, testified that due to its own initiative KG&E has managed to save approximately $5 million dollars for 1986, on a net of tax basis. Staff, through Mr. Ostrander, testified that KG&E has "made a strong case for the proposition that it be allowed to retain the benefits of cost cutting measures that it has initiated." (Ostrander prefiled direct testimony, p. 20, line 15-18). We agree with staff, and

approve KG&E's request as to the retention of benefits from cost-cutting measures.

36. KG&E has also requested the authority to retain the benefits of economic refinancing of its debt and preferred stock charges. KG&E states that it has aggressively taken advantage of declining interest rates so that the company has saved approximately $20 million. Staff, through Mr. Ostrander, took the position that these savings are not the result of particularly innovative or creative actions of KG&E, but merely the result of federal policy initiatives. Traditionally, this Commission has believed that absent compelling rationales, savings due to declining interest rates should flow through to ratepayers. However, when this component of the plan is balanced against the other factors of the plan, such as the insurance revenues, rate delays and reductions and the likelihood of no further Wolf Creek related rate increases outside of this order, we find the request to retain the benefits of economic refinancing to be reasonable. However, the Commission has determined that KG&E shall update annually the cost of debt to actual which is reflected in the carrying charge and deferred revenues calculation. This matter is further elaborated on later in this order.

37. KG&E also requests the authority to retain the benefits of the 1986 Tax Reform Act. This particular provision of the plan raises important concerns for the Commission. Indeed, this Commission is initiating a generic docket which will deal with the issue of retained tax savings due to the Tax Reform Act. KG&E argues in its application and testimony that the retention of tax savings is critical to the success of the plan. Staff, in the alternative, argued that KG&E will incur no risk if the tax rates increased, while retaining all of the benefits if

tax rates decreased. Additionally, staff suggested an interesting threshold analysis which could be used in future rate cases. (Ostrander prefiled direct, p. 22-24). Traditionally, this Commission has believed that utility rates should reflect actual tax rates, not tax rates that are higher (which unduly benefit the utility) or lower (which unduly benefit the ratepayer), than actual. The Commission still believes in this policy.

However, this plan presents the issue of tax savings in a different manner. Along with the tax savings, KG&E proposes to allocate $800 million of its own revenues, and delay rate increases which will save ratepayers $80 million, and reduce the space heating rate resulting in another $20 million in rate savings to ratepayers. Additionally, KG&E maintains that it can live within the constraints of this plan so that no future Wolf Creek related rate increases will be necessary. While the tax benefit issue, if viewed in isolation seems at odds with established Commission policy when the issue is placed in context as a part of a creative, innovative plan that purports to generate significant benefits to both ratepayers and KG&E, the analysis used by the Commission, and ultimately the results reached, must be different. Therefore, as a part of this comprehensive plan, and indeed specifically conditioned upon the other rate payer beneficial aspects of this plan, the Commission approves KG&E request as it relates to tax law savings.

However, the Commission believes that any additional tax savings above those anticipated by KG&E should be considered for return to the ratepayers. Therefore, during the period 1987 through 1992, KG&E is directed to file with the Commission by April 1, of each year a report which shows the increase to its previous year's operating

income which result from benefits of the Tax Reform Act of 1986. If, during these years, the actual benefits as reported by the company and after investigation and confirmation by staff, exceed the amounts projected by KG&E (Exhibit 1, Schedule EDP-6), the excess shall be subject to refund, perhaps on a cumulative basis if the circumstances warrant. If there are any refunds, the refund shall include an interest charge using the authorized rate for consumer deposits. We would expect that an especially careful review would occur prior to the presently scheduled rate increase on January 1, 1989.

38. The Company, in its application, requests that it accrue the debt component of deferred carrying costs for the physical excess portion of Wolf Creek on a "before tax basis," and accrue carrying costs on deferred phase-in revenues on a "before tax basis." By its application, KG&E has asked that the preferred equity component of this accrual be eliminated. Additionally, the plan calls for KG&E to cease the accrual of carrying charges on excess capacity on December 31, 1991, and on January 1, 1992, begin to amortize those costs to cost-of-service using a sinking fund method over the remaining depreciable life of Wolf Creek. Further, KG&E asks the Commission to reconfirm its decision regarding accelerated amortization of construction related tax credits found in Docket No. 149,109-U. As can be readily seen, these aspects of the plan are intricate, and to a large degree merge into other aspects of the plan, specifically ratable capacity addition and a determination of the depreciable life of Wolf Creek.

The Commission does, at this time, reconfirm our earlier decision regarding construction tax credits found in Docket No. 149,109-U. We also find the KG&E request

as stated above to be reasonable and appropriate for the following reasons and with the following changes. This Commission realized when it formulated the original Wolf Creek orders that eventually the issue of amortizing the accumulated deferral cost related to excess capacity back into cost of service would have to be dealt with. Although this particular amortization mechanism was not what we had envisioned, we are pleased that KG&E has found a method to deal with this issue that does not result in an increase in rates to KG&E customers. In regard to the accrual portion of this mechanism, we find the KG&E request reasonable with two modifications. First, we find that staff's recommendation that the cost debt component be updated to accurately reflect the current cost of debt to have a great deal of merit.

Second, we find that KG&E should reflect the actual preferred cost of equity in its accrual charge. Therefore, KG&E is permitted to accrue carrying charges on the physical excess capacity portion of Wolf Creek on a before tax (gross) rate which reflects KG&E's actual cost of debt and preferred stock as determined annually from its official annual report to the Commission (Form No. 1). This accrual will cease on December 31, 1991, and on January 1, 1992, will be amortized on a sinking fund basis over Wolf Creek's remaining life.

39. When considering the comprehensive nature of the proposed Plan, KG&E's request to extend Wolf Creek's depreciable life to 40 years is reasonable. Ample foundation exists in the record of Docket No. 142,098-U to support this change. Although KG&E stipulated to a Staff proposed depreciation rate for purposes of the Wolf Creek rate case, KG&E did so without implication as to the useful life of the plant. Based on the evidence in the record,

the Staff proposal was only one of a number of reasonable approaches the Commission could have adopted. Indeed, in the Wolf Creek orders we noted that we could readdress this issue in the future, and did not foreclose the use of alternative depreciation rates. Given the design, construction and operation and maintenance of Wolf Creek, it is reasonable to find that its operating life could be 40 years. We also note that KG&E's Nuclear Regulatory Commission operating license for Wolf Creek covers a period of 40 years. KG&E is directed to establish a composite annual depreciation rate of 2.61 percent, based upon a 40 year depreciable life, for its investment in Wolf Creek.

40. KG&E is ordered to amortize over five years the deferred asset of $6.4 million representing the allowed cost of operating Wolf Creek between the commercial service date and the effective date of the Wolf Creek rate Orders. Implicit in the creation of this deferred asset was the requirement that the asset would eventually be charged back to cost of service. Under KG&E's Plan, however, the Commission finds that this asset can be amortized to the Kansas jurisdictional cost of service over the next five years without requiring additional revenue from ratepayers.

41. In the Wolf Creek rate Order, we found that KG&E had generating capacity in excess of peak plus reserve of 327 megawatts. Consequently, 327 megawatts of the capacity of Wolf Creek was found to represent excess physical capacity. In support of its application to make interim charges permanent, KG&E calculated its excess capacity to be 223 megawatts, using the methodology found in the Wolf Creek rate Orders. In those Orders, we had determined that a five year forecast period for

peak demand was reasonable given the facts that were before us, and therefore selected 1990 as the reference year for the calculation of excess capacity. KG&E used the five year forecast method of analysis in its Application for permanent rates to be consistent with the Wolf Creek rate orders and to reflect the passage of one year from the time of those Orders. Though we agree that 1991 is the proper reference year for determining KG&E's need for capacity with respect to this application, we note that KG&E's actual normalized peak demand in 1986 was 41 MW below KG&E's own forecasted peak. While KG&E's application to make interim charges permanent assumes that 100 percent of Ripley capacity is excluded, it also assumes that KG&E's actual normalized peak in 1986 would equal its forecasted peak. The 41 MW shortfall in the actual peak virtually balances the incremental 46 MW attributable to Ripley. Since we found the retirement of Ripley was reasonable, prudent, under the methodology used in the Wolf Creek rate Orders we find that the excess portion of KG&E's Wolf Creek capacity is 269 MW. Although 269 MW of excess capacity is significant, and normally would be excluded from cost of service, we believe that KG&E's plan successfully deals with our concerns. KG&E's plan calls for the ratable inclusion of capacity so that at the end of five years (December 31, 1991) KG&E would have no excess capacity attributable to Wolf Creek. Further, KG&E states that the ratable inclusion of capacity will not result in a rate increase outside of those increases granted in this order. It is interesting to note that KG&E's load forecasts show that if the Commission were to still use the five year projected load method of calculating excess capacity, all of KG&E's current excess capacity would be used by the mid 1990s. However, even with the likelihood of future load growth,

if this aspect of the plan were analyzed in isolation it would not meet the criteria established in Wolf Creek rate order. Under KG&E's plan, however, the benefits of rate stability combined with the other beneficial aspects of this plan allow the Commission to find that the reduction of excess capacity by 53.8 MW on January 1 of each year through 1991 to be reasonable. The Commission further notes that when this provision is combined with the amortization of deferred costs associated with excess capacity, a potential problem to both ratepayers and shareholders has been solved to the benefit of both ratepayers and shareholders.

42. In light of the Commission's approval of KG&E's plan for coping with the problems associated with the Wolf Creek Plant, we believe a few additional requirements are in order. There is little doubt that construction of unneeded or excessively expensive generation causes enormous difficulties for utilities and rate payers. One obvious lesson of Wolf Creek is that utilities need to aggressively pursue programs which efficiently manage the timing and need for generation. This responsibility complements the Company's obligation to provide efficient and reliable service without any lapse. This Commission has regularly expressed its belief that various Demand Side Management programs, such as conservation, time of use rates, and load management should be given equal status with Supply Side Planning. KG&E's Load Management Control Program is of particular interest to the Commission because of the significant impact it could have in lowering and controlling growth of the Company's summer peak demand. The Commission notes with approval that KG&E currently has over 5,400 residential and commercial customers participating in its load management program, providing KG&E with up to 11 MW of load management.

The Commission believes that KG&E should aggressively seek and attain its self-established corporate goal of 100 MW of peak shaving capability. We therefore require that KG&E report in writing to the Commission and staff, by December 15 of each year: (1) KG&E's existing load management capability; (2) the anticipated addition to that capability for the next year; (3) the current corporate goal, with an explanation of why it is less than 100 MW, or why it cannot be higher than 100 MW; (4) a listing of promotional/educational efforts in the past year by KG&E to let customers know the details of the load management program, as well as an update on how those efforts will be increased or perfected in the coming year; (5) the amount by which the previous year's summer peak demand was reduced through utilization of the company's load management program; (6) the estimated in-service date and estimated capacity of new plant additions over the next 10 years, and; (7) a copy of the economic analysis supporting the type of generation favored versus the reasonably available alternatives. In addition, the company shall submit by June 1 of each respective year the Load and Capability Forecast for that year. Also, the Commission encourages KGE to work with Kansas Electric Utilities Research Program (KEURP) regarding load management.

43. KG&E, in its application, requests that we revalue Wolf Creek from our previously determined value of $1290 per KW to the full cost of $2376 per KW. In the original Wolf Creek rate orders we stated that at the value of $2376, Wolf Creek was an economically inefficient and excessively expensive means of providing electricity to ratepayers. Furthermore, we found that full rate base inclusion of Wolf Creek at $2376 per KW would not reflect economic efficiency in that its generating capacity could

have been provided at a more reasonable cost to ratepayers. Thus, while we allowed full recovery of the cost of construction of Wolf Creek (except the prudence adjustment, which is analyzed in paragraph 44), we were determined to share the risk of this excessively expensive plant between shareholders and ratepayers. Therefore, we determined that while the utilities could receive a return on the value of $1290 per KW through rates, the ratepayers would not contribute to the return on the costs over $1290 per KW.

Since the determination of $1290 as the value of Wolf Creek resulted from an analysis of the relative cost efficiencies of nuclear and coal plants, we expected to revisit the issue of the value of Wolf Creek and the division of risk for uneconomical plant between ratepayer and shareholder at a later date. In the application before us, KG&E has proposed a method for dealing with the issue of value in a way that deals successfully with our concerns of risk sharing. KG&E proposes to increase the value of Wolf Creek to $2376 per KW while at the same time not requiring rate increases beyond what is contemplated in this order. Although there is no firm basis for reassessing the cost efficiencies of Wolf Creek, there is a sense in which the value of the plant has increased. Since the KG&E plan contemplates no further rate increases, it could be said the plant is more beneficial to rate payers. Further, a higher valuation will allow KG&E to improve its financial situation. Therefore, to the extent that KG&E can improve its financial situation while holding the line on rate increases, both KG&E and ratepayers benefit from the increase in value of Wolf Creek from $1290 per KW to $2376 per KW. Of course, if the predicates to the revaluation were to change (i.e., rate stabilization, benefits to ratepayers and shareholders, etc.), the analysis of this

Commission could also change. Additionally, consistent with this finding, KG&E is also permitted to accrue carrying costs on Wolf Creek's excess capacity valued at $2376 per KW.

44. In the Wolf Creek rate Orders, the Commission found that $128 million of KG&E's share of Wolf Creek construction costs was inefficiently and imprudently incurred. As part of its Plan, KG&E is now requesting an above the line amortization of its Commission determined imprudent investment in Wolf Creek over the plant's remaining depreciable life. KG&E does not seek a rate of return on the undepreciated portion of the imprudence disallowance. The Commission expressly reaffirms its finding that $128 million of KG&E's investment in Wolf Creek was inefficiently and imprudently incurred. Amortization above the line to cost of service, however, is justifiable under KG&E's Plan because it will not require increases in rates above the levels contemplated by the Wolf Creek rate Orders and this Order. As a component of this Plan, and specifically conditioned on implementation of the other aspects of this plan which are beneficial to ratepayers, KG&E will be allowed to amortize above the line the previously disallowed imprudent portion of its investment in Wolf Creek over the plant's remaining depreciable life. We note that while K.S.A. 66-128e prohibits a return on costs which we have found to be imprudent, K.S.A. 66-128c permits us to exercise discretion in allowing a return of those costs. From the ratepayers' perspective, as long as such costs do not require an increase in rates, the fact that they were originally imprudently incurred is of less significance. This, of course, is not the case if return of such costs would result in rate increases. In such an event, our prior disposition of imprudent costs would be appropriate.

45. Finally, KG&E has restated its request that the first and second increases under the phase-in plan approved in the Wolf Creek rate Orders be made permanent. In the Wolf Creek rate Orders, we found that the initial rate increase under our phase-in plan should be interim in nature until six months of actual operating results for Wolf Creek became available. More than six months of Wolf Creek operations have occurred. Mr. Prothro testified that the cost of operating and maintaining Wolf Creek during its first year of operation was approximately $77 million while the projected O & M expense utilized in the Wolf Creek rate Orders was approximately $65 million. Uncertainties about the operation of Wolf Creek and the level of Wolf Creek O & M expenses have been resolved and, therefore, it is reasonable to permit the first two increases to become permanent.

46. The Commission's findings and conclusions in this Order should not be construed as surrendering or limiting the broad authority to review and evaluate the efficiency or prudence of any actions of KG&E, as such authority is granted to it under K.S.A. 66-128, *et seq.* Nor should this Order be construed as a finding that KG&E's prudent investment in Wolf Creek will not be subject to regulatory review at any time in the future should unexpected contingencies occur in either KG&E's proposed Plan or its operations. As pointed out by KG&E in its Application, any changes or modifications to the operation of this Plan or any other increase in rates cannot be implemented without prior Commission approval.

47. It must be emphasized that our approval of KG&E's Plan is premised on no rate increases other than those set forth above. This is particularly true of the cost of service treatment afforded Wolf Creek costs but includes

all the various accounting and ratemaking elements of the plan. Although we find these requests reasonable as part of KG&E's effort to improve its financial situation without further rate increases, reconsideration of all the elements would be necessary in the event of any request to increase rates. Furthermore, in such an event, it would be incumbent on KG&E to prove the reasonableness of all elements of its cost of service. Of course, the Commission also continues to have the right to reexamine all elements of KG&E's revenue requirements should it appear that its earnings or rates are unreasonably high.

IT IS, THEREFORE, BY THE COMMISSION ORDERED AND ADJUDGED THAT:

1. KG&E is permitted to combine $800 million of its projected stream of income in excess of premium expense from corporate owned and shareholder funded life insurance with utility operating revenue to cover its Kansas jurisdictional cost of service. This cost of service includes a return on KG&E's prudent investment in Wolf Creek.

2. KG&E is permitted to:

   (a) Delay from September 27, 1987, to January 1, 1989, the third increase approved in the Wolf Creek rate Orders and will add to such increase any revenue impacts resulting from the Commission finding in Docket No. 142,098-U regarding retirement of its Ripley Station.

   (b) Delay from September 27, 1988, to January 1, 1992, the fourth increase approved in the Wolf Creek rate Orders.

   (c) Spread the third and fourth increases on an equal percentage basis to each component of each schedule.

(d) The third and fourth increases are to be permanent and spread on an equal percentage basis to each component of each rate schedule.

3. KG&E is authorized to reduced its current rate for residential and farm electric space heating customers for usage which exceeds 650 KWHs per month and for all-electric apartments, 500 KWHs per month, during the non-summer months from 7.14¢ per KWH to 5¢ per KWH.

4. KG&E is required to report in writing to the Commission and staff, by December 15 of each year: (1) KG&E's existing load management capability; (2) the anticipated addition to that capability for the next year; (3) the current corporate goal, with an explanation of why it is less than 100 MW, or why it cannot be higher than 100 MW; (4) a listing of promotional/educational efforts in the past year by KG&E to let customers know the details of the load management program, as well as an update on how those efforts will be increased or perfected in the coming year; (5) the amount by which the previous year's summer peak demand was reduced through utilization of the company's load management program; (6) the estimated in-service date and estimated capacity of new plant additions over the next 10 years, and; (7) a copy of the economic analysis supporting the type of generation favored versus the reasonably available alternatives. In addition, the company shall submit by June 1 of each respective year the Load and Capability Forecast for that year.

5. KG&E is permitted to retain the benefits of cost cutting measures, economic refinancings and the new federal tax law. If during the period 1987 through 1991 KG&E's actual increases in operating income due to the benefits of the Tax Reform Act of 1986 exceed those levels

found in Exhibit 1, Schedule EDP-6, the excess shall be subject to investigation and refund if circumstances warrant. KG&E is directed to file a report with the Commission by April 1 of each year through 1992 which shows the increase to its previous year's operating income which results from the benefits of the Tax Reform Act of 1986 when compared to the previous tax law. Such report shall be calculated and presented as requested by staff.

6. Docket No. 149,109-U is consolidated with this Docket.

7. The authority granted to KG&E in Docket No. 149,109-U to accelerate to eight years the amortization of construction related tax credits, as more fully described in that Docket, is reaffirmed.

8. KG&E is permitted to accrue carrying charges on the portion of Wolf Creek which the Commission finds constitutes excess physical capacity. Such accrual will be at KG&E's before tax (gross) cost of debt and preferred stock adjusted annually and shall be applied to KG&E's investment of $2,376 per KWH.

9. KG&E is permitted to accrue deferred phase-in revenues at a before tax (gross) rate until the delayed third rate increase becomes effective on January 1, 1989. KG&E is also permitted to accrue carrying charges on these accumulated revenues until the delayed fourth rate increase becomes effective on January 1, 1992. The carrying charges are to be based on a 15.5 percent cost of equity and KG&E's actual cost of debt and preferred stock adjusted annually. These carrying charges are to be compounded semiannually. KG&E is not permitted to accrue deferred phase-in revenue related to the incremental impact of Ripley's retirement.

10. KG&E is permitted to cease accrual of all deferrals and carrying charges on December 31, 1991, and thereafter amortize the deferrals and carrying charges on a sinking fund basis over Wolf Creek's remaining depreciable life.

11. KG&E is permitted to extend Wolf Creek's depreciable life to 40 years and to establish a composite annual depreciation rate of 2.61 percent for its share of Wolf Creek.

12. KG&E's previous Application requesting that interim charges for electric service be made permanent in this Docket is approved.

13. KG&E is permitted to amortize over the next five years the deferred asset of $6.4 million representing the allowed cost of operating Wolf Creek during the period beginning with the commercial service date and ending with the effective date of the Wolf Creek rate Orders.

14. Under the methodology of the Wolf Creek rate Orders, KG&E's excess physical capacity in Wolf Creek is 269 MW. Beginning January 1, 1988, such excess shall be reduced consistent with the findings of this order.

15. KG&E will be permitted to amortize the undepreciated portion of the $128 million of its investment in Wolf Creek previously determined by this Commission to be imprudent. The amortization period will be Wolf Creek's remaining depreciable life.

16. KG&E's Plan permits rate recognition of KG&E's investment in Wolf Creek beginning January 1, 1992.

BY THE COMMISSION IT IS SO ORDERED.

Lennen, Chm.; Wright, Com.; Henley, Com.

Dated: March 11, 1987

/s/ Judith McConnell
Judith McConnell
Executive Director

SEAL
RLB:rh

ORDER MAILED MAR 11 1987

TRANSCRIPT OF HEARING

(Docket Nos. 142,098-U and 149,109-U)

* * *

Q. Mr. Haines, and I will, as Mr. Moline did, acknowledge that this is perhaps outside the scope of your rebuttal testimony, but it occurred to me this afternoon that during your testimony the Writ of Certiorari you filed with the United States Supreme Court was not discussed. What's the effect on your appeal of the Commission's order if the plan is approved?

A. My belief is that there is no effect. I'm sure that counsel for the Commission will consider the possibility of a different position.

Q. Well, then, would I be correct, then, in assuming that if you got relief from the United States Supreme Court, you would feel that you could come back to the Commission for relief, then, immediately?

A. No.

Q. Is that another quantifier on the plan?

A. No, it isn't and it never has been. We have said publicly right from the start that our appeal of the Wolf Creek rate orders would not change or alter the strategy that we have been following to attempt to re-establish our financial health.

Q. Okay, thank you.

A. Whether we fail or succeed.

MR. IRBY: Thank you, no further questions.

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